BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Gregory Scott	Chair
Edward A. Garvey	Commissioner
Marshall Johnson	Commissioner
LeRoy Koppendrayer	Commissioner
Phyllis A. Reha	Commissioner

In the Matter of Qwest Corporation's Refiling of its Proposed Tariffs Regarding Termination Liability Assessments as Applied to Resale Arrangements

ISSUE DATE: October 2, 2001

DOCKET NO. P-421/AM-00-1165

ORDER REJECTING TARIFF/PRICE LIST REVISIONS

PROCEDURAL HISTORY

This is the third in a series of related cases dealing with the termination liability assessments (TLAs) that Qwest Corporation proposes to charge long-term contract customers who choose to substitute a reseller for Qwest as the provider of contract services.

The first case was a complaint proceeding. In that case a competitive local exchange carrier with extensive resale operations claimed that high TLAs charged by Qwest violated federal law, its interconnection agreement with Qwest, and the public interest. The Commission issued an Order construing Qwest's tariffs and finding that, under the tariffs' terms, TLAs did not apply when customers substituted a reseller for Qwest in extended term contracts.[1] The Company appealed this decision to the Minnesota Court of Appeals.

The Company also filed new tariff and price list revisions which explicitly imposed TLAs on customers substituting a reseller for Qwest in long-term contracts. This filing began the second case, in which the Commission ultimately rejected the TLAs at issue on grounds that they were not just and reasonable, that they functioned as barriers to competition, and that they unduly and unreasonably restricted the resale of contract service arrangements.[2] The Company appealed this decision, too, to the Minnesota Court of Appeals.

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[1] In the Matter of a Complaint by InfoTel Communications, LLC v. U S WEST Communications, Inc. Concerning Resale of Contract Services, Docket No. P- 421/C-98-10, ORDER CONSTRUING TARIFFS AND PROHIBITING TERMINATION CHARGES IN RESALE CONTEXT (May 21, 1998).

[2] In the Matter of U S WEST Communications, Inc.'s Proposed Revisions to Termination Liability Assessments, Docket No. P-421/EM-98-769, ORDER REJECTING TARIFF/PRICE LIST REVISIONS, CLARIFYING PRACTICAL EFFECT OF FILING, AND STAYING IMPLEMENTATION OF FUTURE TARIFF/PRICE LIST REVISIONS (October 13, 1998).

On May 4, 1999 the Minnesota Court of Appeals reversed and remanded the Commission's decision in the first case. The Court rejected the Commission's finding that the original tariff language itself prohibited the application of TLAs in resale situations. The Court also found that the Commission had reasonably concluded that the purpose of the tariff was cost recovery, and the Court therefore remanded the case for specific findings on costs and other relevant factors.[3] The Court noted that the second appeal had been filed and said that "the end of this litigation does not appear to be in sight for either party."

The litigation did end shortly, however, under a stipulation signed by the parties on June 10, 1999. Under the stipulation Qwest agreed that it would

(a) file another tariff on the application of TLAs in resale situations, different from the one under appeal in the second case; and

(b) dismiss its appeal in the second case;

while the Commission agreed that it would

(a) act on the new filing by conducting an expedited proceeding under Minn. Stat. § 237.61, unless a different kind of proceeding was required by law; and

(b) either delegate the filing to a Commission subcommittee under Minn. Stat. § 216A.03, subd. 8 or designate a lead Commissioner for the filing under Minn. Stat. § 216A.03, subd. 9.

On August 17, 2000 Qwest filed its new proposed tariffs, which are at issue in this case, together with supporting documents and legal memorandum. These tariffs would impose a TLA of 17.66% of the monthly contract rate for each month the customer did not take service directly from Qwest during the first year of the contract, with that rate dropping to 9% during subsequent contract years. To qualify for these TLAs, which are lower than those that can apply outside the resale context, the reseller serving the customer must agree to buy the contract services at wholesale from Qwest for the remainder of the contract term.

The Company stated that the purpose of the TLAs was to recover the retail costs it had already incurred but not yet recovered when customers switched to resellers.

Comments opposing the proposed tariff were filed by the following parties: the Minnesota Department of Commerce; the Residential and Small Business Utilities Division of the Office of the Attorney General; Eschelon Telecom of Minnesota, Inc.; McLeodUSA Telecommunications Services, Inc.; EN-TEL Communications, LLC, Lakedale Link, Inc., WH Link, LLC, and Direct Communications, LLC, filing jointly; the Association of Communications Enterprises (ASCENT), formerly the Telecommunications Resellers Association; USLink, Inc.; and Firstcom, Inc.

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[3] <u>InfoTel Communications, LLC v. Minnesota Public Utilities Commission</u>, 592 N.W.2d 880 (Minn.App. 1999), *rev denied* (July 28, 1999).

The parties opposing the new tariffs claimed that they did not meet statutory standards of fairness, reasonableness, and non-discrimination; that they would function as barriers to competition, violating state and federal law; and that they would unduly and unreasonably restrict the resale of contract service arrangements, violating state and federal law.

On January 8, 2001, the Commission issued an Order designating Chair Scott lead Commissioner in this case and authorizing him to conduct evidentiary hearings on the issues listed below, and any related relevant issues.

(a) the amount of Qwest's unavoided costs when a retail customer taking service under a long term contract switches to a reseller buying wholesale service from Qwest;

(b) the reasonableness and likely consequences of the proposed tariff provision making resellers liable for the wholesale rate for the remainder of a customer's contract term, whether the customer completes the contract term or not;

(c) whether the TLAs proposed by Qwest constitute unreasonable restrictions on resale;

(d) whether all Qwest TLAs in a resale setting should be prohibited as anti-competitive, as unreasonable restrictions on resale, as contrary to public policy, or on any other grounds, and if so, whether this prohibition should be temporary or permanent.

Chair Scott conducted evidentiary hearings on March 26, 2001. Due to changes in circumstances and business plans, some parties had withdrawn from the case. The remaining parties were Qwest; the Minnesota Department of Commerce; the Residential and Small Business Utilities Division of the Office of the Attorney General (RUD-OAG); and four competitive local exchange carriers, filing jointly: EN-TEL Communications, LLC, Lakedale Link, Inc., Direct Communications WH Link, LLC, and Direct Communications, Inc.

The parties filed pre-hearing and post-hearing briefs. Qwest filed a post-hearing amended proposal in response to concerns raised at the evidentiary hearing. Qwest also filed a motion for leave to file a reply memorandum and supporting affidavit, together with that motion and affidavit. The Commission granted Qwest's motion, which was unopposed, and accepted its reply filing.

The Commission met to hear arguments from the parties and to deliberate on July 24, 2001.

FINDINGS AND CONCLUSIONS

I. Introduction and Background

A. The Long-Term Contracts at Issue

This case involves long-term contracts for five product groups or groups of telecommunications services –

- PBX (Private Branch Exchange), a computerized, on-site service that routes calls within organizations with multiple telephone lines;
- Centrex, a computerized, off-site service that routes calls within organizations with multiple telephone lines;
- ISDN (Integrated Services Digital Network), a network configuration permitting the end-user to transmit voice, data, and video over a common line;
- Intrastate Private Line Service, a direct circuit or channel dedicated to connecting a specific end-user to a designated point or points;
- Advanced Communications Services, a group of highly specialized services including Frame Relay Service, ATM Cell Relay Service, MegaBit Services, and Local Area Network Switching Service.

Under these long-term contracts, customers agree to purchase a service for a specific length of time, in exchange for a discounted price. Contracts run from three to ten years -- the longer the term, the steeper the discount. And, most important for present purposes, the contracts impose TLAs if the customer stops taking service directly from Qwest before the end of the term.

B. Qwest's Resale Obligations

Under state and federal law Qwest must permit competitors to interconnect with its network on competitive and non-discriminatory terms and must permit competitors to purchase its services at wholesale and resell them at retail.[4] Both state and federal law also prohibit Qwest from imposing unreasonable or discriminatory restrictions or limitations on the resale of its wholesale services.[5]

Qwest offers the five services at issue here on a wholesale basis, both as month-to-month services and as long-term contract services. The wholesale rate is 17.66% below what Qwest charges at retail for the same month-to-month or long-term contract service.

This 17.66% wholesale discount rate, which applies to all Qwest's wholesale services, was set by the Commission in an earlier proceeding. As required by federal law, it represents the percentage of retail costs (marketing, billing, collection, and other costs) that Qwest avoids when it sells a service at wholesale instead of at retail.[6]

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[4] 47 U.S.C. § 251(c); Minn. Stat. § 237.16.

[5] 47 U.S.C. § 251(b)(1); 47 U.S.C. § 251(c)(4); Minn. Stat. § 237.121 (a)(5).

[6] 47 U.S.C. § 252(d)(3).

II. Qwest's Proposal

A. The Original Proposal

The Company originally proposed a TLA of 17.66% of the monthly contract rate for each month the customer did not take service directly from Qwest during the first year of the contract term. The TLA would drop to 9% per month for subsequent contract years. These TLAs, which are lower than those assessed when a customer stops taking contract services entirely, would apply only if the reseller agreed to buy the contract services at wholesale from Qwest for the remainder of the contract term.

Qwest based its TLA calculations on the 17.66% wholesale discount set by the Commission for Qwest's wholesale services across-the-board. The Company began with the assumption that that discount accurately reflects the costs the Company normally avoids when it sells services wholesale rather than retail. The Company then stated that converting long-term retail contracts into long-term wholesale contracts is not the same as selling wholesale from the beginning, because in the conversion case the Company has already incurred retail costs – especially sales and marketing costs – which the wholesale discount properly treats as avoided.

The Company therefore used the wholesale discount as a starting point for calculating the costs it avoids when it converts long-term retail contracts to long-term wholesale contracts. It used the cost categories the Commission had used to set the wholesale discount and adjusted them to reflect the retail costs it had already incurred when contracts were converted from retail to wholesale.

The Company's cost analysis determined that, while the Company avoids 17.66% of its retail costs in pure wholesale transactions, it avoids only 4.96% of its retail costs when it converts a long-term wholesale contract to a long-term retail contract. This difference requires the Company to charge a TLA of 12.7% of the face amount of the contract to recover its costs.

The Company's cost expert explained that, instead of charging 12.7% across-the-board, the Company decided to discourage early contract terminations by charging 17.66% per month during the first year of the contract and 9% during later years. Her calculations indicated that this two-tier TLA policy would produce the 12.7% overall recovery rate her cost data supported.

B. The Post-Hearing Proposal

In its post-hearing brief the Company dropped its proposal to charge different TLAs for different years of the contract term and lowered its estimate of its total unavoided retail costs from 12.7% of the retail rate to 11.93% of the retail rate. The lower rate was offered in response to evidence from the RUD-OAG that the 12.7% rate failed to take into account Miscellaneous Revenues, which the Commission had taken into account in calculating the wholesale discount on which the Company based its TLA calculations. The Company emphasized that it was offering the lower rate as a compromise, not as an admission of error.

The Company also offered an additional compromise proposal in which contract customers substituting resellers for Qwest would pay the lower of the 11.93% overall TLA or a service-specific TLA, which would reflect only the retail costs not avoided for that specific service. Under this proposal, the TLAs for the five services (or groups of services) at issue would be as follows:

PBX	7.75%
Centrex	11.93%
ISDN	11.93%
Intrastate Private Line	7.07%
Advanced Communications	11.93%

The Company also urged the Commission to treat this case as a civil court would treat a breach of contract case, using the record to fashion an appropriate remedy if the Company failed to prove its entitlement to all it sought.

III. Parties' Responses

A. Department of Commerce

The Department of Commerce (the Department) urged the Commission to reject the Company's proposal on grounds that incumbents cannot charge TLAs when customers switch to resellers without violating state and federal laws prohibiting unreasonable restrictions on resale. The agency classified all TLAs as restrictions on resale, emphasized that the Federal Communications Commission has found all restrictions on resale presumptively invalid,[7] and argued that the TLAs in this case are not narrowly tailored enough to defeat the presumption of invalidity.

The Department also argued that it was not fair, reasonable, or in the public interest to permit the use of TLAs when other cost recovery methods that would not inhibit competition to the same degree were readily available. (The Department suggested higher up-front charges or higher monthly rates.)

Finally, the Department claimed that the Company's TLA calculations were conceptually flawed and empirically unsound.

B. Residential and Small Business Utilities Division of the Office of the Attorney General (RUD-OAG)

The RUD-OAG did not agree with the Department that TLAs were unreasonable restrictions on resale *per se*. The agency believed that the TLAs in this case, however, both imposed unreasonable restrictions on resale and failed to meet statutory standards of fairness, reasonableness, and non-discrimination.

The agency argued that the cost calculations on which Qwest based its TLAs were unsound in theory and in application, chiefly for the following reasons:

- the cost development process was driven by the Company's legal and policy staff, not its cost staff;

[7] *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, First Report and Order, CC Docket 96-98, FCC 96-325 (rel. Aug. 8, 1996), ¶ 939.

- Qwest's calculations were based on cost data that included both month-to-month and long-term contract customers;
- Qwest's calculations were based on costs that included the costs of marketing to persons who decided not to take long-term contract services;
- Qwest's calculations failed to credit sales commissions refunded on terminated contracts;
- Qwest failed to present evidence distinguishing its unavoided costs in the long-term contract context from its unavoided costs in the month-to-month context;
- Qwest failed to establish its actual costs and actual profit margins for long-term contract services.

The agency also contended that Qwest discriminated against resellers and their customers by imposing TLAs on customers terminating long-term contracts to take more expensive service from resellers, while waiving TLAs for customers terminating long-term contracts to take more expensive service from Qwest.

C. The EN-TEL Group

Four competitive local exchange carriers – EN-TEL Communications, LLC, Lakedale Link, Inc., Direct Communications, and WH Link, LLC – filed joint comments opposing the proposed TLAs. They stated that TLAs in this range made it impossible for them to compete for Qwest's existing long-term contract customers and threatened the viability of resale as a market entry strategy by "locking up" the lucrative long-term contract services segment of the market.

They argued that it was unduly discriminatory for Qwest to waive TLAs for customers upgrading to a more expensive Qwest service, but not for customers upgrading to a more expensive service from a reseller. Similarly, they challenged what they claimed was Qwest's practice of determining on a case-by-case basis whether it would impose TLAs on a terminating customer.

They contended that it was unfair and unreasonable for the proposed tariffs to require resellers to pay "standard" TLAs of up to 40% if their customers stopped taking service entirely.

They claimed that Qwest's cost calculations were fundamentally flawed, for the reasons given by the Department and the RUD-OAG, and because (1) Qwest's calculations failed to distinguish between marketing costs for new and renewed contracts, and (2) Qwest made no adjustments for cost savings from long-term contracts, only for cost increases.

IV. The Commission's Historical Treatment of TLAs

Long-term contracts and the TLAs that go with them have been a conundrum since local competition began. On the one hand, consumers and businesses can benefit from the significant discounts long-term contracts provide. On the other hand, consumers, businesses, and the economy as a whole may be harmed if long-term contracts act to thwart competition by "locking up" lucrative segments of the emerging market. The Commission's historical treatment of TLAs has reflected the difficulty of balancing these competing interests.

In May 1996 the Commission rejected a proposal by Qwest (then U S WEST) to offer long-term contracts with TLAs of 15% to 25%, on grounds that those contracts posed a threat to the competitive market the Commission had a duty to nurture:

> The rate stability plan clearly gives U S WEST an unearned competitive advantage over other companies which may wish to enter the SingleNumber Service market. [footnote omitted] It permits the Company to capture market share now, before effective local exchange competition has been realized, by offering discounted prices, and to retain market share later, as competitive forces evolve, by enforcing exit penalties in the long term contracts required to get the discounted prices. This marketing strategy and its resulting competitive advantage are available to U S WEST only because it is currently the monopoly provider.
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> To allow U S WEST or any other incumbent provider to exploit its monopoly status and throw up eleventh hour barriers to customers changing companies would directly contravene state and federal policies opening the local telecommunications market to competition. It would complicate, prolong, and perhaps jeopardize the already complex process of transforming a monopoly environment into an effectively competitive one. It would be unfair to competitors, who cannot yet extract long term commitments in return for rate reductions.
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> In the Matter of U S WEST Communications, Inc's Proposal to Offer a Rate Stability Plan for SingleNumber Service, Docket No. P-421/EM-95-1245, ORDER REJECTING RATE STABILITY PLAN (May 7, 1996).

In March 1997 the Commission found that the competitive market had evolved to the point that it was reasonable to permit Qwest to offer long-term contracts for specialized services with TLAs of 15% to 30%.[8] The Order emphasized that no one had opposed the contracts at issue and that the Commission retained the right and duty to intervene on behalf of the public interest if necessary.

By October 1998, however, it was clear that a thriving competitive market was still a goal, not a reality, and that long-term contracts with high TLAs and other anti-competitive features were one of many factors stalling competition:

> While the Commission may have been right in believing that contracts could encourage competition by permitting business customers to use familiar procurement methods to buy telecommunications services, the length of these contracts (up to 10 years) and the size of their termination charges (up to 40%) have eliminated any pro-competitive effect they might have had. They do, as the Commission originally feared, "lock up" the market at a time when consumer options ought to be burgeoning.
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> Furthermore, the automatic renewal provisions of these contracts can lock up small or inattentive customers beyond the original contract term, compounding their anti-competitive effect. The contracts' failure to identify the services

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[8] In the Matter of a Request by US WEST Communications, Inc. for Authority to Introduce a Rate Stability Plan for the Service Configuration Element of ISDN Primary Rate Service, Docket No. P-421/EM-96-1419, ORDER APPROVING PETITION (March 20, 1997).

contracted for as competitive, or to otherwise signal the existence of competitive alternatives, can also confuse or mislead less sophisticated customers.

In short, these contracts, at least as applied to resale customers, function as barriers to competition at this stage in the development of the competitive market. They therefore fail the "just and reasonable" standard of Minn. Stat. §§ 237.60 and 237.63. They also unduly and unreasonably restrict the resale of contract service arrangements, in violation of Minn. Stat. § 237.121 (a) (5) and 47 U.S.C. § 251(b)(1).

In the Matter of U S WEST Communications, Inc.'s Proposed Revisions to Termination Liability Assessments, Docket No. P-421/EM-98-769, ORDER REJECTING TARIFF/PRICE LIST REVISIONS, CLARIFYING PRACTICAL EFFECT OF FILING, AND STAYING IMPLEMENTATION OF FUTURE TARIFF/PRICE LIST REVISIONS (October 13, 1998) at 7.

V. Commission Action

(a) Introduction

For these TLAs to be approved, Qwest must prove –

(a) that they are fair and reasonable under Minn. Stat. §§ 237.06, 237.011 (2), and 237.082;
(b) that they are not unduly discriminatory under Minn. Stat. §§ 237.60; and
(c) that they do not impair competition or unreasonably restrict resale under Minn. Stat. § 237.121 (a) (5) and U.S.C. § 251(b)(1) and 47 U.S.C. § 251(c)(4).

To prove these things, Qwest must show that the proposed TLAs reflect the actual retail costs that the Company does not avoid when it converts long-term retail contracts to long-term wholesale contracts. It must show that the non-price terms of the contracts are fair, reasonable, non-discriminatory, and not likely to impair competition. It must show that any TLAs ultimately proved to be cost-justified do not contravene the public interest by impairing the development of a free and competitive market or unreasonably restricting resale.

Since the Company has failed to make these showings, the Commission must reject its TLA proposal.

B. The Company's Cost Evidence Is Flawed, Incomplete, and Untrustworthy

The threshold issue in this case is whether the TLAs proposed by the Company have a solid factual basis. The Commission finds that they do not.

As explained above, the Company used the wholesale discount as the starting point for calculating the costs it avoids when it converts long-term retail contracts to long-term wholesale contracts. It used the retail cost categories the Commission had used to set the wholesale discount and adjusted them to reflect the retail costs it had already incurred but not yet recovered when these contracts were converted from retail to wholesale.

These calculations led the Company to conclude that, while it avoids 17.66% of its retail costs in pure wholesale transactions, it avoids only 4.96% of these costs when it converts a long-term retail contract to a long-term wholesale contract.[9] The Company explained this striking disparity by stating that it incurs most of the retail costs of long-term contracts up-front, mainly in marketing costs, and especially in sales commissions.

The Commission finds that the Company's cost analysis is insufficiently accurate, detailed, and rigorous to support its TLA proposals.

One of the most serious flaws in the cost analysis is that it is not based on data specific to long-term contract services, but on aggregate data on sales and marketing costs of both month-to-month and long-term contract retail customers. There is no reasonable basis to conclude that a TLA based on this methodology will limit Qwest's recovery to unrecovered costs for long-term contract customers. Clearly, the costs of month-to month service and long-term contract service differ; if they did not, the Company could not offer the significant price discounts it offers in long-term contracts.

Using aggregate data to calculate long-term costs simply requires too much guesswork to support the precise cost calculations necessary in this case. The record provides no reliable factual basis for making precise distinctions between long-term contract and month-to-month costs. The Company's TLA claims, however, rest on those distinctions, which it uses to make adjustments in the retail cost categories used in the wholesale discount methodology.

Furthermore, using aggregate data on long-term contract and month-to-month customers means that cost differences between these two classes of customers are already reflected to some degree in the baseline numbers that are being adjusted. Without a reliable way to extract the specific costs attributable to long-term contract customers, there is a significant risk of double adjustments.

Equally concerning, all of the adjustments Qwest made to the wholesale discount cost categories favored Qwest – all of them reflected instances in which the incurred-but-unrecovered retail costs of terminated long-term contract services exceeded the retail costs of month-to-month services. None of them reflected instances in which some retail costs attributable to contract customers were lower than retail costs attributable to month-to-month customers.

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[9] The Company later increased this 4.96% cost figure slightly, to reflect the "Miscellaneous Revenues" originally missing from the equation, as pointed out by the RUD-OAG.

There are clearly many such instances, however, since it is the economies associated with establishing long-term customer relationships that enable the Company to offer the discounted prices of long-term contracts. As EN-TEL points out, these economies would appear to include reduced costs in the areas of billing, collection, and ongoing administrative support, but in the absence of more rigorous cost studies, it is impossible to know for sure.

It also appears that Qwest failed to factor in to its TLA calculations some cases in which sales commissions on terminated contracts – its major unavoided retail cost – were refunded. Similarly, the Company failed to demonstrate that it properly accounted for the reduced marketing costs associated with contract renewals. Further, until it filed its revised, post-hearing proposal, the Company failed to demonstrate that its TLA calculations had properly accounted for the miscellaneous revenues factored into the wholesale discount. And the RUD-OAG also noted that Qwest included as non-avoided costs, the costs of marketing to potential customers who do not take the service.

The Company also failed to establish that its marketing expenses, including its sales commissions, were reasonable in amount and in their terms and conditions of payment.

In short, the accuracy and precision necessary to support a TLA proposal, with its inevitable potential for inhibiting competition, is absent here. In fact, at some points the Company's proposal loses sight of the need for cost justification altogether.

For example, Qwest's original proposal to charge higher TLAs during the first year of the contract had no cost basis and was admittedly designed to discourage customers from switching to resellers early in their contract term. Similarly, the Company filed essentially no cost evidence to support the extremely high TLAs it proposed to charge resellers whose customers terminate service entirely before the end of the contract term.

Further, the Company's post-hearing alternative proposal to dramatically reduce the TLAs for two of the five services – significantly reducing its total TLA collections – casts doubt on the precision of its original proposal, which was presumably designed only to recover total unavoided retail costs.

C. The Proposed TLAs Are Not Fair and Reasonable, are Anti-Competitive, and Unreasonably Restrict Resale

For the reasons explained above, the Commission finds that the Company's cost evidence is not detailed, accurate, or reliable enough to support a finding that the proposed TLAs constitute just and reasonable rates, which the Commission must ensure under Minn. Stat. §§ 237.06, 237.011 (2), and 237.082. The Commission rejects them on that basis.

The Commission also rejects them as unreasonably restricting resale under Minn. Stat. § 237.121 (a) (5) and 47 U.S.C. § 251(b)(1) and (c)(4). Resale is a critical market entry tool for new competitors and a critical network completion tool for established competitors. Unconstrained resale is essential to the development of a competitive local telecommunications market. For this reason, federal law makes all restrictions on resale presumptively invalid.[10]

Similarly, federal law imposes more stringent resale requirements on incumbents than other local exchange carriers (including the duty to sell at cost-based wholesale rates), because it is the incumbents' networks that must be opened for competition to succeed.[11] Qwest's affidavit detailing the TLAs charged by its non-incumbent competitors therefore has little if any bearing on the reasonableness of its own TLAs.

Any tariff affecting resale therefore triggers the highest level of scrutiny from this Commission. Here, the lack of detailed and credible cost support for the proposed TLAs, which will clearly inhibit resale to some degree,[12] require their rejection, as does the Company's failure to establish that the costs its TLAs are designed to recover are reasonable in amount and in their terms and conditions of payment. The Commission therefore will not reach the Department's claim that *all* TLAs are inherently anti-competitive and unreasonably restrict resale.

Finally, although this case has focused heavily and appropriately on the cost justification for the TLAs proposed by the Company, it is important to note that all the terms and conditions of long-term contracts, not just their price terms, must be fair and reasonable, non-discriminatory, and not unreasonably restrictive in their effect on resale. In the second TLA case in this series,[13] the Commission found that specific long-term contract provisions – lengthy contract terms, automatic renewals without notice, failure to identify services as competitive – compounded the contracts' anti-competitive effects. It is not clear from the Company's filing that these concerns have been effectively addressed. To the contrary, the proposal to impose the TLAs on resellers if the ultimate customer defaults further compounds their anti-competitive effect.

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[10] *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, First Report and Order, CC Docket 96-98, FCC 96-325 (rel. Aug. 8, 1996), ¶ 939.

[11] 47 U.S.C. § 251(c)(4).

[12] Although it seems inarguable that high termination fees will discourage customers from terminating contracts with Qwest to take service from resellers, the Department has provided three affidavits illustrating TLAs' real-life effects. In all three cases, TLAs had a clear negative impact on competition. See the Department's filing of February 27, 2001.

[13] In the Matter of U S WEST Communications, Inc.'s Proposed Revisions to Termination Liability Assessments, Docket No. P-421/EM-98-769, ORDER REJECTING TARIFF/PRICE LIST REVISIONS, CLARIFYING PRACTICAL EFFECT OF FILING, AND STAYING IMPLEMENTATION OF FUTURE TARIFF/PRICE LIST REVISIONS (October 13, 1998).

Similarly, it is not clear that the Company has exhausted its rate design options for mitigating the anti-competitive effects of TLAs in long-term contracts. Currently the Company uses two methods to collect the up-front costs of long-term contracts – it amortizes them over the full contract term or it charges a TLA. There are other options, however – higher initial fees, higher monthly fees, deposits – and it is not clear that they have been adequately explored.

For all these reasons, the Commission finds that the proposed TLAs do not meet statutory standards of fairness and reasonableness and that they unreasonably restrain the resale of Qwest's wholesale services.

D. The TLA Proposal Is Unduly Discriminatory

The government agencies and the competitive local exchange carriers who intervened in this case argued that it was unreasonably discriminatory for Qwest's tariffs to waive TLAs for contract customers who terminate their contracts to take a more expensive service from Qwest, but not for contract customers who terminate their contracts to take a more expensive service from a reseller. The Commission agrees.

The record does not demonstrate any cost basis for treating these two classes of customers differently. The Company's sunk and unrecovered retail costs would appear to be the same whether a customer terminates a long-term contract to sign a more expensive contract with Qwest or with a reseller. In the absence of countervailing evidence, the Commission concludes that this tariff term discriminates against upgrading customers choosing a resale provider, violating state statutes prohibiting undue discrimination[14] and state and federal statutes prohibiting unreasonable restrictions on resale.[15]

Furthermore, Qwest's inability to document its grounds for waiving the TLAs in 226 of the 483 termination cases it was able to identify is worrisome, given the high potential for discrimination posed by TLAs.

E. The Commission Cannot Modify the Company's Proposal

The Company urged the Commission to use the record and its own judgment to establish an alternative TLA level, if it felt compelled to reject the Company's proposal. The Commission cannot do this for several reasons.

As explained above, this record lacks the accuracy and precision necessary to support any level of TLA. The tariff language is at points unduly discriminatory. It is not clear that contract terms and conditions previously deemed anti-competitive have been corrected. The reasonableness of the costs for which recovery is claimed has not been established. The potential to use rate design to mitigate the most anti-competitive effects of TLAs has not been fully explored. The Department's claim that all TLAs are unreasonable restrictions on resale has not been decided.

For all these reasons, the Commission declines to set a TLA policy for Qwest on this record.

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[14] Minn. Stat. § 237.60.

[15] Minn. Stat. § 237.121 (a) (5) and 47 U.S.C. § 251(b)(1) and 47 U.S.C. § 251(c)(4).

ORDER

1. The tariff/price list revisions filed by Qwest on August 17, 2000 and amended in its post-hearing comments are hereby rejected.

2. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar
Executive Secretary

(S E A L)

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